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CALFED Water Transfer Element

Draft Discussion Paper No. 9 - Third Party Impacts

Issue

A major set of issues related to water transfers, particularly out of basin, long term (multi year) transfers, is third party impacts. Generally, there are three types of third party impacts: impacts to other legal users of water (usually downstream users); environmental impacts; and economic effects in the source area. This paper deals with third party economic impacts of transfers. Cumulative impacts of a series of one year transfers or multiple long term transfers from the same area raise a special set of third party impact issues. This issue will be discussed in a separate paper.

Applicable Law

Impacts to downstream users are addressed by the "no injury" rule. The "no injury" rule prohibits transfers which would harm another legal user of the water proposed for transfer. This rule is found at Water Code sections 1706, 1725, 1736 and 1810(d).

The "no injury" rule is the legal mechanism for the prohibition of transfers of "paper water" (water which does not meet the test of consumptive use).

State law also prohibits transfers which would have an unreasonable impact on fish, wildlife, or other instream uses. See Water Code sections 1025(b), 1725, 1736 and 1810(d). A similar prohibition applies to CVP transfers subject to the CVPIA.

Economic impacts of transfers are less clearly regulated. It is generally recognized that certain types of transfers can have adverse impacts on local economic conditions. Fallowing transfers, for example, will result in lower agricultural production in the source area and may impact local employment of farm workers and others.

Groundwater transfers or transfers of surface water with groundwater replacement may result in lower groundwater levels, lower groundwater quality and higher pumping costs for other local groundwater users. In extreme cases, impacted groundwater users may lose the use of existing wells due to water quality degradation or lower groundwater levels. (Groundwater issues are discussed in more detail in Issue Paper No. 7. This paper does include some discussion of the potential impacts of groundwater transfers.)

State law does not generally address the economic impacts of fallowing or groundwater transfers. Section 1810(d) provides that the conveyance facilities of a public agency (state, regional

or local) may not be used to transfer water if the transfer would have an "unreasonable effect" on the local economy. The term "unreasonable effect" is not defined.

Section 1745.05(b) of the Water Code limits fallowing transfers by water suppliers to twenty percent of the water that would have been applied or stored by the water supplier, absent the transfer.

Water Code Section 1745.10 prohibits replacement of transferred surface water with groundwater unless certain conditions are satisfied, i.e., consistency with local groundwater management program, or a finding of no contribution to long term overdraft of groundwater.

CVPIA prohibits the Secretary of Interior from approving a transfer which would have a long term impact on groundwater conditions or which would unreasonably impact the water supply, operations, or financial condition of the transferor district or its water users.

Water Code sections 1215 and 11460 prohibit transfers which would deprive areas of origin of water reasonably required to meet local beneficial needs.

However, there is no counterpart of general application in state law to the "no injury" rule or the "no unreasonable environmental impact" rule for economic impacts of fallowing or groundwater based transfers.

Discussion

The fundamental policy issue related to economic impacts of transfers is to what extent should external impacts be internalized as transaction costs of the transfers. How should such costs be calculated? Who should decide which costs are part of the transfer cost? Who decides what level of adverse impact is significant or unreasonable? Ultimately, this leads to a debate about who should have the authority to approve, disapprove or condition a proposed transfer?

Generally these questions will arise in transfers based on land fallowing or crop shifting, or in transfers involving increased use or pumping of groundwater. True conservation transfers (reductions in irrecoverable losses) probably do not generate the same level of third party impacts because they do not affect the level of production or economic activity in the source water area.

There is a range of approaches to the question of how to deal with economic impacts of water transfers. At one end of the range is the view that a purely market based approach to water transfers should not concern itself with external economic impacts. A water rights holder or

water user is under no legal obligation to provide employment or economic benefits to his/her community. No one would argue that a farmer must farm his/her land every year in such a way as to generate a given level of employment or economic activity in the local area. No one would argue that if a landowner sells a parcel of land, that he or she must compensate others who are affected by the change to the local economy resulting from a change in use of the land. According to this logic, then, a farmer or water supplier who sells the right to use water should have no obligation to constrain his/her action due to adverse economic impacts to others and society should not interfere with the operation of the market.

An alternative view is that water transfers should operate in a more regulated environment, based on the concept that water is not a pure commodity, but is in the nature of a shared natural resource, to which an entire community (or region, watershed or basin) has some claim of right. Water "per se" is legally owned by the people of the state and an individual user has only the right to the use of so much as can be put to reasonable and beneficial use. While transfers are recognized under state and federal law as a reasonable and beneficial use, a pure market approach to water transfers fails to acknowledge that entire communities and local or regional economies rely on the economic value produced by the local use of water. Therefore, changes in purpose or place of use of water which affect local socio-economic conditions must be regulated to avoid or mitigate adverse impacts. While this latter view is probably more widely accepted, it still leaves open a number of questions regarding the scope and kind of protection which should be provided against third party economic impacts.

Third party impacts may also occur when the transfer is a direct groundwater transfer or when surface water is replaced with groundwater and there is no recharge or replacement (conjunctive use) program. Here there is a direct impact on a resource which is legally defined as subject to correlative rights (the right of all overlying users to make reasonable and beneficial use of the groundwater). The use by one directly affects the use by another. If one user is allowed to sell or pump groundwater to the detriment of other overlying users, the correlative right can be impaired or destroyed. As noted above, state law proscribes certain types of groundwater transfers which contribute to groundwater overdraft, but does not address economic impacts.

Possible Options

Over the past few years, a number of mechanisms have been suggested for dealing with the local economic impacts of water transfers. Some of the possible tools or options are:

- an agreed upon definition of "third parties" (who are the parties who have a recognizable impact?)

- limits on the number of acres which can be fallowed (in order to produce transfer water) in a given area (District or county);

- limits on the amount of water which can be transferred from a given area (District, service area, county);
- a tax on transfers to compensate the local area for increased social service costs incurred by local governments;
- a mitigation fund for compensating losses or to pay for retraining farm workers, to be administered by local governments;
- a mitigation or compensation fund for those who incur higher groundwater pumping costs as a result of a transfer;
- further restrictions on groundwater transfers or groundwater substitution (e.g., establish a limit on groundwater level drawdown);
- legislation to define level of acceptable impacts of transfers.
- a central "clearinghouse" to collect and disseminate information on transfers and transfer impacts.